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RECEIVED

April 6, 1998

Mr. David S. Guzy
MMS/WRO/RPS
Denver Federal Center, Building 85
Mail Stop 3021
West 6th and Kipling Streets
Denver, CO. 80225

RE: MMS Supplementary Proposed Rule Establishing Oil Value for Royalty Due on Federal Leases ("MMS Second Supplement Notice") (dated February 6, 1998)

Dear Mr. Guzy:

Vastar Resources, Inc. (Vastar) appreciates this opportunity to comment upon the Minerals Management Service (MMS) proposal noticed on Febrary 6, 1998 establishing a new method for valuing crude oil for purposes of calculating royalty due on federal leases. Vastar is a large independent producer headquartered in Houston, Texas. Vastar's stock is publically traded, and 82 1/2% of its outstanding shares are held by the Atlantic Richfield Company (ARCO). Vastar owns no refineries, and its principal business is the finding, producing and marketing of crude oil, other liquid hydrocarbons, and natural gas in the lower 48 states of the United States. Its production is largely in the Gulf of Mexico, San Juan Basin and the Mid-Continent region. Vastar produces and markets approximately 40,000 barrels of crude oil a day. Although Vastar's primary focus is upon marketing its own production, it also maintains an active crude oil trading organization which buys, resells or exchanges barrels produced by third parties. Vastar could be adversely affected by the proposed rule change and therefore wishes to express its views.

Vastar substantially supports the comments of the Independent Petroleum Producers of America, the Domestic Petroleum Council, the American Petroleum Institute and the Rocky Mountain Oil and Gas Association, and therefore will not belabor points discussed more extensively in those trade association filed comments. In Vastar's view, MMS's proposed valuation rules are needlessly complex, burdensome and cumbersome to administer and need to be greatly simplified. Moreover, the agency in these rules is attempting to extract more than the fair value of crude oil at the lease because the rules presume crude should be valued on the basis of various market prices at various market centers or aggregation points, but fail to recognize appropriate deductions to the wellhead of the various location and quality differentials, and other factors of enhanced value, which occur when production is aggregated at market centers.

In part, the difficulty with the proposed rules stems from MMS's continuing overbroad definition of an affiliate transaction. It is compounded by the extraordinarily burdensome tracing requirements imposed upon a lessee who falls into the catagory of making a non-arms length sale, or one who engages in exchanges.

In Vastar's case, although Vastar disposes of most of its crude in arms-length transactions (at least under commonly used definitions of that term), it sells some of its crude to its parent company, the Atlantic Richfield Company (ARCO). These sales typically take place at trading or aggregation centers such as at St. James. At St. James in a given month, Vastar might have dozens of arms-length sales and a few sales of like quality crude to ARCO. ARCO may also be buying multiple barrels from multiple Sellers at St. James. Vastar's price for like quality sales to arms-length third parties or ARCO's price for purchases from arms-length third parties should be an appropriate benchmark for the value of crude sold to ARCO at the same time and location. Either of these sets of prices would be good market indicators of the prevailing market value of crude at St. James. But under MMS's proposed rules, Vastar would have to develop elaborate accounting systems to attempt to track what ARCO did with the barrels after purchasing them from Vastar. This would be a particularly difficult, if not impossible, undertaking. ARCO typically aggregates the barrels it buys from Vastar with thousands of barrels it purchases from hundreds of other crude oil sellers, transports or exchanges those barrels into the Cushing, Ok. market, and makes sales from its aggregated supplies at Cushing to hundreds of different purchasers. Indeed, because of the ambiguous language of the proposed regulations, Vastar might be required to trace barrels for royalty valuation purposes if ARCO is trading barrels (unbeknowst to Vastar) in the same market center with unrelated parties even if Vastar was not selling its barrels to ARCO. Trying to trace the particular destination of Vastar's barrels after they went into ARCO's huge inventory would be like trying to find a needle in a haystack. The burden of compliance with the proposed regulations as to affiliated sales or exchanges may be so great that Vastar would have to stop selling to ARCO, even where ARCO is offering a better price than that offered by arm-length third parties. Similar difficulties arise in tracing exchange barrels.

Vastar questions the utility of imposing these onerous tracing burdens on exchanged volumes and on transactions with affiliates. If index or spot prices reported at various trading or aggregation centers are appropriate benchmarks of value for certain purposes, as the MMS appears to conclude in its proposed regulations, then it would seem these index or spot prices should also be the final measure of value for barrels exchanged with others, or traded to an affiliate, at those aggregation centers. The MMS could then focus on developing a workable, simple system for deducting appropriate transportation expenses, and accounting for location and quality and other differentials, to net back to a proper lease value. Vastar is concerned that the MMS's burdensome tracing requirements go far beyond what might reasonably be required to calculate an appropriate wellhead value for federal production, and instead are designed so that the MMS can extract as much as possible of the earnings which a crude oil trader might realize through undertaking downstream risks and providing downstream value added services, without sharing in any of those risks or costs. In the example of multiple sales and purchases at St. James, market value for like kind barrels could readily be obtained by looking at comparable sales. The only reason MMS would seem to have for tracing barrels to Cushing or other post-St. James transactions, would be to enable MMS to obtain more than the St. James market value. In short, it would be done for the purpose of allowing MMS to benefit from any Cushing price upgrades without taking any of the Cushing trading risks or costs.

Vastar supports and echoes the call by RMOGA and others for MMS to implement quickly a comprehensive Royalty in Kind program that would give the industry certainty, and allow a producer to have closure on his royalty obligations after production. Promulgating vague, confusing, complex and burdensome valuation regulations now will only result later in numerous valuation disputes on audit years after production, as producers and the agency contest the interpretation and application of various regulatory provisions in specific transactions.

Respectfully Submitted,

VASTAR RESOURCES, INC.

Norma J. Rosner
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